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Supreme Court of the United States

October Term, 1975

No. 75-853

UNITED STATES STEEL CORPORATION and
U. S. STEEL HOMES CREDIT CORPORATION,
Petitioners,

vs.

FORTNER ENTERPRISES, INC.,
Respondent.

On Writ of Certiorari to the United States
Court of Appeals for the Sixth Circuit

REPLY BRIEF FOR THE PETITIONERS

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REPLY BRIEF FOR THE PETITIONERS

Introduction

Respondent Fortner's brief, apparently because of misconceptions as to the issues raised by petitioners, misstates and distorts those issues.

Throughout its brief (pp. 2, 15-17, 20-21, 29, 33, 37-39, 51-52), Fortner argues that with respect to the question of sufficient economic power over credit essential to applica-

tion of the *per se* tying rule only issues of disputed fact are to be resolved, a function not undertaken by this Court. Fortner states (p. 2) that in the 1975 appeal from the second trial "the question before the Sixth Circuit was whether the District Court's *fact finding* of economic power was clearly erroneous" and that "no real legal issues were before the Sixth Circuit * * *." (Fortner's emphasis) Concededly, petitioners did urge below that many of the trial judge's findings (adopted verbatim when he signed a photocopy of Fortner's proposals) were clearly erroneous,[1] but they also raised the very same issues now presented to this Court. The Court of Appeals expressly recognized that fact, stating that "The most significant [argument advanced on appeal by the defendants] involves the question of whether the district court applied the proper legal criteria for determining the economic power issue." (A 1763)

In similar vein, Fortner urges (pp. 15, 17-18) that in its 1969 decision this Court "held that Fortner had made a *prima facie* case of violation of Section 1 of the Sherman Act." In support of that contention, Fortner quotes, out of context, Justice Black's statement for the majority that "We therefore conclude that the showing made by [Fortner] was sufficient on the market power issue."[2] To the contrary, all that the majority of this Court held was that on the summary judgment record then before it, "read in

1. Petitioners here raise no question under Rule 52(a), F.R.C.P., but instead limit their contentions to showing that Fortner failed to make out any *prima facie* case of violation of the Sherman Act and that, in holding to the contrary, the courts below misconceived and failed to apply the legal standards mandated by this Court.

2. *Fortner Enterprises, Inc.* v. *United States Steel Corp.*, 394 U.S. 495, 506 (1969).

the light most favorable to" Fortner because "summary judgment in antitrust cases is disfavored," Fortner's allegations sufficiently "raised questions of fact" to entitle it to a trial inasmuch as its claims "may suggest," "can reflect" or were not inconsistent with "the possibility of market power over borrowers in the credit market * * *."[3] As Justice Black stated:

> "Under these circumstances the pleadings and affidavits sufficiently disclose the possibility of market power over borrowers in the credit market to entitle [Fortner] to go to trial on this issue. * * * It may turn out that the arrangement involved here serves legitimate business purposes and that U. S. Steel's subsidiary does not have a competitive advantage in the credit market. But on the record before us it would be impossible to reach such conclusions as a matter of law, and it is not our function to speculate as to the ultimate findings of fact. We therefore conclude that the showing made by [Fortner] was sufficient on the market power issue." (394 U.S. at 500, 504-506)

Even the Court of Appeals so read this Court's earlier decision. (A 1372-73, 1378-80, 1383-84, 1765-66)

Fortner also mistakenly argues throughout its brief that petitioners are asking this Court "to take back its 1969 decision in this case." (pp. 15-17, 19, 24, 31-33, 35) To the contrary, petitioners' objective here is solely to demonstrate that the courts below have failed to follow this Court's mandate and that, applying the legal standards set forth in this Court's earlier decision, Fortner has simply

3. As noted at pp. 21-22 of petitioners' principal brief, the four dissenting Justices, differing as to the proper summary judgment standards, forcefully disputed this conclusion by the majority. (394 U.S. at 514-516, 518-520)

failed to make out a *prima facie* case of econômic power over the tying element, credit, or any violation of the Sherman Act. Petitioners respectfully submit that respondent, having ignored or misunderstood this Court's mandate during the course of two plenary trials, is the party seeking to rewrite that earlier decision to accommodate its failure of proof.

Finally, Fortner's brief is remarkably barren of record citations to support its broad and sweeping conclusions. In fact, the record is devoid of evidence to support the arguments which are fundamental to Fortner's position. To avoid prolonging this reply brief, petitioners will treat those evidentiary failings only in connection with discussion of Fortner's claims as to why the lower courts' conclusion of economic power over credit should be sustained.[4]

1. While This Court Held Proof That Either Legal Barriers or a Unique Cost Advantage Prevented Other Lenders From Making Equally Favorable Loans Was Essential to Establish the Requisite Economic Power Over Credit, Fortner Mistakenly Argues That a Variety of Evidentiary Elements Will Suffice.

In its prior decision, this Court explained that the economic power essential to the *per se* tying rule arises from uniqueness in an attractive commodity only because

4. In one or two instances where the conclusions urged are premised upon evidence taken out of context and are therefore misleading, petitioners outline the record proof merely in the Appendix to this reply brief inasmuch as proper disposition of the legal issues upon which this case turns would be the same even if those conclusions urged by Fortner were supported by the evidence. As noted in their principal brief (p. 6), for purposes of this Court's review petitioners do not rely upon any evidence which was disputed on the trial record.

competitors are either physically or legally precluded from offering the self-same product or because they are economically prevented by a favored seller's unique cost advantage from profitably selling that product at his price. Money is a fungible commodity and a loan, therefore, can be unique only in the sense that it is offered on cheaper, more favorable terms than available elsewhere. Consequently, this Court held that proof of power over credit or unique competitive advantage in that market required evidence that other lenders were unable to grant equally cheap or attractive loans at a profit because of legal barriers or because petitioners enjoyed a unique cost advantage. The issue mandated by the Court was not whether comparably cheap, favorable loans were *unavailable* elsewhere at the time petitioners financed Fortner but rather, in Justice Black's words, whether the "Credit Corporation had a *unique economic ability* to provide 100% financing at cheap rates" because petitioners had "achieved economies of scale in their credit operations" so that others "could not profitably lend money on the risks involved" or because they were legally prevented from offering comparable terms.[5] (394 U.S. at 505-506, 509)

5. In addition to those commentaries cited in petitioners' principal brief (p. 29) which have understood this Court's prior opinion in this case as petitioners do, a former Assistant Attorney General in charge of the Antitrust Division, Edwin M. Zimmerman, has publicly analyzed the decision as follows: "* * * [W]hat market power means is that you do not have to cut your price [for the tying commodity]; that you can, in fact, raise your price or in lieu thereof, require the tie. * * * [W]hat the majority had in mind * * * is the notion that U.S. Steel alone was able to offer this type of credit because its competing financial institutions were barred by legal regulation * * * [or], as an alternative possibility * * *, [that U.S. Steel] could have lowered its prices on credit substantially and still made a profit * * * in a way that its competitors could not emulate. * * * [O]n remand, U.S. Steel would be free to prove that all it was doing

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Fortner disputes this analysis (p. 19), urging that "there simply is no way that you can read [this Court's opinion] to limit the proof to those narrow elements" and that, instead, Justice Black "enumerated a number of standards or elements of evidence which possibly alone or in combination among themselves would establish the requisite 'sufficient economic power.'" Obviously, the Court will decide for itself which view of its earlier decision is correct. Petitioners will not repeat the details of Justice Black's analysis here other than to note several of Fortner's contentions which highlight its misreading of that decision, including those several purported "elements of evidence" which Fortner claims are competent to prove economic power over credit and which it asserts (pp. 19, 29-31) were found by the courts below to establish that power.

2. Uniquely Advantageous Loan Terms Are Not Proof of Economic Power in the Credit Market.

Fortner contends (pp. 31-32) that uniquely advantageous loan terms are evidence of economic power over credit. As evidentiary support for this conclusion, Fortner relies heavily, if not exclusively (pp. 13-14), upon its proposed findings (adopted verbatim by the trial judge) characterizing the purported testimony of its expert witness, Professor Masten. Those findings are that *at the particular*

was cutting its price and that competitors could have done so as well, in which case, it has no power. The plaintiff could prove that U.S. Steel was in a unique position either because of regulatory restraints on its competitors or because it had unexercised market power in that it had certain advantages which others simply could not emulate." Panel Discussion, "Recent Trends in Supreme Court Antitrust Decisions: Commentary—Past, Present and Future," 38 Antitrust L.J. 602, 615 (1969)

time of its loans to Fortner[6] the Credit Corporation, in Professor Masten's opinion, "had economic power by granting terms to the borrower that were so distinctly unique that it was almost inconceivable that the funds could have been acquired from any other source"[7] and that "the Credit Corporation had definite leverage in the segment of the credit market related to land acquisition and development loans as a lender because of the uniqueness of the terms of the loans made * * *."[8] (A 1593-97)

6. Not only did Professor Masten limit his testimony as to the unavailability of 100% land loans to the period of the challenged Fortner loans, admitting that to his knowledge conventional lending sources made such loans in later periods (A 1637-39, 1642, 1659-62), but even plaintiffs' findings adopted by the trial court perforce confine the temporal limits of his testimony of uniquely favorable terms to just "that time," "for the period of time in question," and so on. (A 1592-97)

7. In fairness to Professor Masten, he did not purport to testify that the Credit Corporation had "economic power" over credit in the sense defined by this Court for purposes of the *per se* tying rule. Asked by Fortner's counsel whether the Credit Corporation had "economic power *of any nature* with regard to the tie-in," Professor Masten answered: "Well, by granting terms to the borrower that were so distinctly unique that it is almost inconceivable that the funds could have been acquired from any other source, then the Credit Corporation had economic [power] *if that is the sense that you are using the term.*" (A 1642)

8. Fortner's brief (pp. 13, 25) also refers to another portion of Professor Masten's testimony relating to the Credit Corporation's allegedly more favorable terms which Fortner included in one of its proposed findings, adopted without change by the trial judge. That finding states that Professor Masten "pointed out that in his opinion 100% land acquisition and development loans of the nature and terms granted to [Fortner] were a segment of the credit market, and that if you only have one lender making such loans within that segment of the market, then that lender has economic power within that segment of the market." (A 1596) Fortner now urges (p. 25) that in such circumstances the sole lender making 100% loans at a given time "has control of or actually monopoly power over that segment of the market." This contention is specious. Even if a properly defined market has only a single seller, that seller does not have

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Concededly, although he admitted having no knowledge either as to what lenders made land loans in 1960 and 1961 or on what terms such loans were actually made, Professor Masten testified that in his *opinion* 100% loans would not have been *available* at the time. (A 1486-91, 1692-93) At no point, however, did he or any other witness claim that the Credit Corporation's land loans to Fortner or any other builder were unique in the sense that all other lenders were *unable* to offer equally favorable, advantageous and cheap loans because of legal, economic or any other barriers. The record is devoid of any such evidence.

Professor Masten's opinion that the Credit Corporation had economic power over credit because its terms to Fortner were supposedly *unavailable* elsewhere is directly contrary to this Court's holding and the views of the dissenting Justices, as well. (394 U.S. at 505, 515, 518) The Court held, instead, that "Uniqueness confers economic power only when other competitors are in some way prevented from offering" the same product or from offering it profitably on the same terms. (*Id.* at 505, n.2) The evidence,

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either monopoly power or any lesser gradient of economic power unless he has some unique cost or other competitive advantage which precludes other sellers from profitably entering that market and competing with him, as the record here shows other lenders did in the 100% land loan "market" defined by Professor Masten. At the same time that he claimed that if a lender is "the only lender making loans under those specific terms" then he has economic power in that market segment or submarket (A 1643), Professor Masten also testified repeatedly that no two loans are the same. (*e.g.*, A 1634, 1652) If all loans are different and therefore each falls into a different market, then it follows, from Professor Masten's opinion, that every lender, every time he lends, has economic power in a market limited to that particular loan. Petitioners submit that whatever the nature of the economic power thus contemplated by Professor Masten, it is not the "sufficient economic power" defined by this Court as essential to invoking the *per se* rubric.

therefore, must show that other lenders were unable to compete by offering comparable financing because barred by some competitive advantage enjoyed only by petitioners.

"Uniquely favorable," cheaper loans not available elsewhere do not prove that the lender is "uniquely able" to make such loans. At most, they merely prompt inquiry as to whether their unavailability elsewhere is attributable to any such "unique ability" or competitive advantage enjoyed solely by that lender.[9] Absent proof of such an advantage, loans on cheaper or more favorable terms merely reflect the lender's willingness to take less than the normal profit demanded by others—just as in this case, where the lower courts concluded and Fortner conceded that traditional lending institutions in Louisville, stimulated to offer 100% land loans soon after the financing of Fortner, had earlier been merely unwilling to risk lower profits. (A 1601, 1768)

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9. Justice Black's opinion for the Court recognized the fact that a low price for the tying element neither proves nor disproves market power and expressly rejected Fortner's contentions. Rather, as Justice Black pointed out, such facts merely "may suggest" or "can reflect" the "possibility of market power." Other evidence, however, is necessary to prove that the seller is able to offer the lower price *because* he has "unique economic advantages" or cost savings not enjoyed by his competitors in the market for the tying element. As Justice Black stated: "We do not mean to accept [Fortner's] apparent argument that market power can be inferred simply because the kind of financing terms offered by a lending company are 'unique and unusual.' We do mean, however, that uniquely and unusually advantageous terms can reflect a creditor's unique economic advantages over his competitors." (394 U.S. at 504-506)

3. Evidence That the Tied Product Is Higher Priced or Otherwise Non-Competitive Is Not Proof of Economic Power Where the Tying Element Is Credit, Unique Only Because Offered on Cheaper, More Favorable Terms.

Fortner also argues (pp. 32-35) that proof of a higher price for the tied product is evidence of economic power over credit[10] and that this Court so held. This Court, however, did not so hold. Rather the majority noted merely that a substantial price differential for the tied product knowingly accepted by the buyer "may suggest" or is not inconsistent with the "possibility of market power," because "in a freely competitive situation buyers would not accept a tying arrangement obligating them to buy a tied product at a price higher than the going market rate * * *." (394 U.S. at 504-506)

Even if the Homes Division's houses were shown to have been higher priced, that is not evidence of economic power where the tying element is cheaper credit—a fungible commodity that can be unique only in the sense that it is offered on cheaper, more favorable terms than available elsewhere. Thus, if Mr. Fortner had believed the houses to be over-priced or otherwise non-competitive at the time he agreed to the tie-in,[11] he would have accepted that burden

10. While Fortner claims (p. 23) that its expert, Professor Masten, "put all of the economic power evidence into full focus and context," he never adverted to the asserted higher price of petitioners' houses or the acceptance of such a tie-in by customers to support his opinion that petitioners had economic power over credit.

11. Respondent's answer (p. 33) to the uncontradicted evidence that Mr. Fortner was affirmatively attracted to the houses themselves and never deemed them higher priced or otherwise non-competitive

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only because he concluded that the saving realized on the allegedly cheaper or more favorable financing compensated for the higher price or burden of accepting the houses and made the "package" of tying and tied elements attractive.[12] Consequently, evidence of higher price for the tied product is at most evidence only that the loan terms were arguably cheaper or more favorable than available elsewhere. That fact—cheaper or more favorable terms—does not prove economic power, because, as this Court held, power over credit can be shown only by evidence that other lenders are *unable* to offer equally cheap or favorable loans owing to legal barriers or a unique cost advantage.

Fortner, however, urges in its supplemental brief (p. 3) that the Second Circuit's recent decision in *Hill* v. *A-T-O, Inc.*, 535 F.2d 1349 (2d Cir. 1976), "recognizes that

until long after he negotiated the loans from the Credit Corporation is the unsupported charge that "the Homes Division people sold Mr. Fortner a bill of goods concerning the house package." This is essentially a concession that petitioners have correctly characterized the evidence as showing that Mr. Forner in no way considered the houses a burden or non-competitive until after he had negotiated not one but two loans from the Credit Corporation. (See pp. 12-14, 34-36 of petitioners' principal brief)

12. For an analogous evaluation of the effect of the claimed higher price for the houses upon such damages as Fortner could properly claim assuming violation, see Areeda, "Antitrust Violations Without Damage Recoveries," 89 Harv. L. Rev. 1127, 1138 (1976) ("The tie in the case was based on the plaintiff's claim and the ultimate finding that [U.S. Steel] offered unusually attractive financing terms that were not otherwise available. That rationale means that the plaintiff was unusually benefited by the arrangement. One would have to subtract that benefit from the incremental sums paid for the houses [above the price of similar houses made by others] in order to determine the extent of the plaintiff's harm. Indeed, unless the benefit equaled or exceeded the increment, a rational person in the plaintiff's position would not have entered into the arrangement at all. And because there is no reason not to, the plaintiff might just as well be assumed to be rational").

evidence of a price for the tied product in excess of similar competitive products and that the tying product was unique and lacked comparable substitutes at the time in question created factual questions concerning economic power which prohibit disposition of the case as a matter of law." Petitioners have no quarrel with that conclusion, because in *Hill* the tying element, for summary judgment purposes, was assumed to be unique in and of itself and not available on any terms from any source other than the tying seller.

In those circumstances, the inference of economic power is permissible from proof that the buyer, at the time he accepts the tying condition, knowingly acquiesces in spite of the fact that he does not want the tied product or deems it non-competitive in price or otherwise. This is true because the buyer's unwilling acceptance of the tie is evidence of the economically coercive power of the unique tying element, at least where the price of that tying element has not been reduced below its regular level. The same inference, however, can not be drawn where, as in this case, the tying element is fungible and "unique" only because offered at a cheaper price. There the resulting saving, without additional proof that any alleged premium paid for the tied product exceeds that saving, vitiates any inference of economic coercion and power in the tying element which might otherwise be argued from the tied product's higher price.[13]

13. Fortner's supplemental brief (p. 3) also asserts that the *Hill* case contradicts petitioners' claimed argument "that coercion is an element essential to be proven to establish economic power." As their principal brief shows (pp. 35-36), however, petitioners make no such argument. Rather the Second Circuit and other cases treated

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Thus, Fortner argues at cross-purposes that economic power is established by an allegedly lower price for the fungible tying element, credit, while at the same time it undercuts that contention by urging inconsistently that the asserted higher price for the tied product is additional proof of the requisite power. The contradictory nature of these arguments is underlined by the fact that, even assuming *arguendo* that Mr. Fortner deemed the Homes Division houses to be over-priced at the time he negotiated the challenged loans, if the asserted overcharge for the houses exceeded the saving from the allegedly cheaper financing then the claimed attraction or coercive inducement of the loans is destroyed. On the other hand, if the claimed overcharge for the houses was less than the saving from the allegedly cheaper financing, then Fortner was more than compensated for the higher price of the houses and the attraction or coercive inducement of the loans is nevertheless reduced, so that it becomes questionable whether there remains any evidence to support even the erroneous contention that cheaper financing proves economic power over credit. In any event, the record is wholly lacking in evidence as to how the saving on the assertedly cheaper land loans compared with the incremental cost incurred from the claimed higher price of the houses.

there were cited for the proposition that, where proof of economic power over a tying product unique *per se* is based upon the buyer's coerced or unwilling acceptance of a tied product he does not want or deems inferior, the fact that he was dissatisfied with and economically coerced to take the tied product must be established as of the time he agrees to the tie-in. The decision in *Hill* relies upon that very principle ("* * * [U]nlike the situation in *Capital Temporaries,* where plaintiff offered no evidence to suggest that he was only interested in obtaining the office personnel franchise or that he objected to taking the 'blue collar' franchise *at the time the license arrangements were made,* * * * [the plaintiffs] in the instant case introduced affidavits stating that they were already the owners of satisfactory vacuum cleaners before entering into contracts with the Compact defendants and were forced to purchase new Compact cleaners in order to obtain the desired [tying product]"). (535 F.2d at 1355)

4. Acceptance of the Tie-In, Even by Many Customers, Is Not Proof of Economic Power Where the Tying Element Is Credit, Unique Only Because Offered on Cheaper, More Favorable Terms.

In support of the contention that acceptance of the challenged tie-in by many customers is evidence of economic power, Fortner urges (pp. 7, 15, 35-40) that numerous tying arrangements similar to its financing were established and that 70% of all sales of houses by the Homes Division "were accounted for by loans involving the tie-in." The record, however, does not show the terms on which any other builder was financed (let alone that those terms were even unavailable from other lenders at the times and places where offered). The claim that the asserted volume of house sales was induced by the 100% land financing challenged by Fortner or by similar financing is also without evidentiary support.[14]

Even if the facts were as Fortner argues, however, such proof is not evidence of economic power over credit. As analyzed in more detail in petitioners' principal brief (pp. 38-40), a tying element consisting of a fungible commodity such as credit offered at a lower price than available elsewhere (and unique only because of that cheaper price) must invariably attract buyers, because competing sellers can not command a higher price for that fungible commodity. Consequently, acceptance of a tied product even by many buyers attracted by the lower price of the tying loan proves only that the loan terms are cheaper, not that the lender has any unique economic or legal advantage

14. The evidence to the contrary is analyzed in some detail in the Appendix to this reply brief at pp. 1a-4a.

which prevents others from offering comparably cheap terms.

Fortner, however, claiming that "We established the ability to raise price and to impose the tie-in on a substantial number of customers" (pp. 19, 24), places heavy reliance (pp. 35-37) upon the statement, isolated from the essential background set forth in Justice Black's majority opinion, that:

> "Accordingly, the proper focus of concern is whether the seller has the power to raise prices, or impose other burdensome terms such as a tie-in, with respect to any appreciable number of buyers within the market." (394 U.S. at 504)

Fortner also relies upon the mistaken reading of that sentence by the Fourth Circuit in *Advance Business Systems & Supply Co.* v. *SCM Corp.*, 415 F.2d 55 (4th Cir. 1969), *cert. denied*, 397 U.S. 920 (1970), citing that decision for the asserted proposition that "the fact that numerous customers had accepted the tie-in • • • [is] conclusive evidence of the requisite economic power." Fortner then urges that "This Court could very well affirm the decision in this case on the basis of *Advance Business Systems* alone." (pp. 36-37) Misuse of the partial quotation from Justice Black's opinion by both Fortner and the Fourth Circuit, however, totally alters the import of what was said by the omission of the immediately preceding relevant and essential text.

Both Fortner and the Fourth Circuit in *Advance-SCM* have failed to read the quoted language in the context of Justice Black's detailed discussion of the fact that with most tying elements (unlike the credit here) market power involves a seller's ability to raise his price, at least to some

customers. This is generally the case, because in most tying arrangements the tying product is different than others and at least some customers regard it as sufficiently unique, distinctive, and attractive to pay a premium over the price of what they deem to be the nearest substitute.[15] Clearly Justice Black was not speaking of a fungible tying product in this portion of his analysis, because no seller can raise his price for such a product above the price his competitors are willing to accept.[16] Ignoring the import of Justice Black's analysis, both Fortner and the Fourth Circuit have omitted the crucial sentence preceding their out-of-context quotation from his opinion. Thus, culminating his discussion of market power as represented by the power to charge at least some customers a higher price for a unique tying product, Justice Black stated:

> "In both instances [*i.e.*, regardless of whether the seller has the greatest economic power possible or merely some lesser degree of appreciable economic power], despite the freedom of some or many buyers from the seller's power, other buyers—whether few or many, whether scattered throughout the market or part of some group within the market—can be forced to accept the higher price because of their stronger preferences for the product, and *the seller could therefore choose instead to force them to accept a tying arrangement* that would prevent free competition for their patronage in the market for the tied product. Accordingly, the proper focus of concern is whether the seller has the power to raise prices, or impose other burdensome terms such as a tie-in, with respect to any appreciable number of buyers within the market." (394 U.S. at 503-504)

15. "* * * [T]he presence of any appreciable restraint on competition provides a sufficient reason for invalidating the tie. Such appreciable restraint results whenever the seller can exert some power over some of the buyers in the market, even if his power is not complete over them and over all other buyers in the market. In fact, complete dominance throughout the market, the concept that the District Court apparently had in mind, would never exist even under a pure monopoly. Market power is usually stated to be the ability of a single seller to raise price and restrict output, for reduced output is the almost inevitable result of higher prices. Even a complete monopolist can seldom raise his price without losing some sales; many buyers will cease to buy the product, or buy less, as the price rises. Market power is therefore a source of serious concern for essentially the same reason, regardless of whether the seller has the greatest economic power possible or merely some lesser degree of appreciable economic power." (394 U.S. at 503)

16. In claiming that it proved petitioners' "ability to raise price," an assertion which, on the record here, can only have reference to the allegedly higher price of the Homes Division houses, Fortner misconceives the language it has quoted from Justice Black's opinion. Justice Black was referring in this portion of the opinion to the power to raise the price of the *tying* product, not the price of the *tied* product.

In other words, Justice Black said, if the seller could have raised the price of the tying element, unique in and of itself, but instead demanded the tie-in in lieu of the higher price, then the requisite power would be shown.[17] He did not say that mere acceptance of a tie-in by customers proves economic power where the tying element is fungible or otherwise incapable of commanding a premium price from at least some buyers.

While Justice Black declared that tying arrangements achieve unlawful restraints only when it is proved that "the seller can exert some power over some of the buyers in the market" (394 U.S. at 503), in the *Advance-SCM* case the

17. See Dam, *"Fortner Enterprises* v. *United States Steel*: 'Neither a Borrower, Nor a Lender Be,'" 1969 Supreme Court Rev. 1, 25-26; see also the analysis of Justice Black's opinion by Edwin M. Zimmerman, formerly Assistant Attorney General in charge of the Antitrust Division, Panel Discussion, "Recent Trends in Supreme Court Antitrust Decisions: Commentary—Past, Present and Future," 38 Antitrust L.J. 602, 615 (1969) (* * * [W]hat market power means is that * * * you can, in fact, raise your price [for the tying product] or in lieu thereof, require the tie").

Fourth Circuit erroneously adopted the circular reasoning that acquiescence in the tying arrangement "by an appreciable number of customers gives rise to an inference that [the seller] had 'some power over some buyers' in the market." (415 F.2d at 69) Such reasoning is totally contrary to logic when applied, as Fortner here urges, in circumstances where the tying element is not itself unique but is wholly fungible (so that no power to raise its price can be inferred) and where the only aspect of uniqueness is that, as alleged here, the tying element is offered at a lower price than available from competitors.

In those circumstances, acceptance of the tie, even by many customers induced solely by the lower price of the tying element, fails to prove power. Such evidence shows instead only that the price of the tying element is in fact lower but not that the tying seller alone has a unique ability to sell at that price.[18] As Justice Black and the majority held, the requisite power must then be shown by proof that competitors in the tying market for credit could not similarly reduce their prices either because legally barred from doing so or because petitioners had a unique cost advantage.

Similarly, Fortner's reliance (p. 36) upon *Northern Pacific Railway Co.* v. *United States,* 356 U.S. 1 (1958), as "an obvious illustration of the fact that evidence of acceptance of the tie-in by a substantial number of customers will be evidence of the requisite economic power" is misplaced. In *Northern Pacific,* the tying product was land, not only inherently unique but, as this Court emphasized, "strategically located" and "frequently essential" to the

18. See Justice White's dissent. (394 U.S. at 518)

businesses of the large numbers of purchasers and lessees who accepted the tying condition there. Even in that situation, the Court limited its conclusion that the "host of tying arrangements" was evidence of power "at least where, as here, no other explanation has been offered for the existence of these restraints" and noted that "the defendant makes no claim that [the tying land] came any cheaper than if the restrictive clauses had been omitted." (356 U.S. at 7-8)

By contrast, here the allegedly cheaper price of the Credit Corporation's financing accounts for and explains the acceptance of the tying arrangement, and acceptance of the tie in those circumstances provides no basis for inferring coercive economic power. In the absence of such power, any cheaper price for the tying element was merely for the legitimate business purpose of promoting the sale of the Homes Division's houses and was tantamount to a reduction in the price of the houses. Thus, as Justice Black recognized, "advantageous credit terms may be viewed as a form of price competition in the tied product," and a seller can achieve such price reduction as long as he offers "fringe benefits over which he has no economic power." (394 U.S. at 508)

5. As Found by the Court of Appeals, the Evidence Fails to Prove That Other Lenders Were Prevented by Legal Regulation From Making 100% or Equally Favorable Land Loans.

While conceding that legal prohibitions against 100% land loans "did not apply to all potential lenders," Fortner claims that such barriers did prevent "a very substantial segment of the potential lenders" from making such loans. Indeed, Fortner even represents that this Court "in 1969

took judicial notice of the fact that *many* lenders were legally barred from making 100% land acquisition and development loans." (p. 26) In fact, all that Justice Black said was that "potential competitors such as banks and savings and loan associations *may* have been prohibited from offering 100% financing * * *." (394 U.S. at 506)

Moreover, even in adopting Fortner's proposals verbatim, the trial court made no evidentiary finding that would support the quantitative sweep of Fortner's claim now that "many lenders" constituting a "very substantial segment of the potential lenders" were legally barred from making 100% land loans. To the contrary, the Court of Appeals examined the record and in its first opinion, while noting that national banks[19] and federally insured savings and loan associations were prohibited from making such loans, concluded:

> "Yet the record appears to be barren of any evidence that other lending institutions in the Louisville area were subject to the same prohibition, such as mutual savings banks, credit unions, pension funds, finance companies, mortgage companies, building and loan associations, and insurance companies. A jury should be permitted to evaluate the significance of the freedom of such traditional lending sources from any restriction against extending 100% financing in deciding whether competitors in the Louisville credit market were precluded from offering credit on such terms." (A 1380)

In its second opinion, the Court of Appeals concluded that "While the court below took notice that national banks and

19. The evidence is undisputed that, as Fortner's expert, Professor Masten, testified, the majority of banks in Kentucky were not national banks and that there were other than national banks in Louisville, as well. (A 1698-99)

federal savings and loan associations were legally prohibited from making 100% loans, there was no similar evidence as to the many other types of lending institutions." (A 1768)

Even more importantly, while Fortner ignores the fact, the Court of Appeals initially found that:

> "Further, while [Fortner] offered some evidence that 100% financing was not generally available on the Louisville market at the time of its financing with the Credit Corporation, it must be conceded that the amount of the loan as a percentage of the collateral or security is only one element in determining its advantage to a borrower. Other relevant factors * * * include the rate of interest charged, whether the lender discounts the amount loaned or charges service or other fees, and the maturity and terms of repayment. Proof alone that an institution is prohibited from granting 100% land financing would therefore seem to be insufficient to establish the fact that it is unable to offer terms embodying other elements which would make its financing equally favorable or advantageous to the borrower." (A 1380-81)

And the Court of Appeals ultimately concluded after the second trial, "Nor was there evidence that any lender was prohibited from varying other terms of loans so as to offer equally favorable financing." (A 1768)

In summary, there is no evidence that at the time of Fortner's financing competing lenders were not legally *able,* if they chose, to offer land financing as favorable as the Credit Corporation's allegedly was. Consequently, in keeping with the mandate of this Court and as found by the Court of Appeals, the record compels the conclusion

that petitioners had no economic power or advantage arising from legal barriers depriving other lenders of the ability to make equally favorable or cheap loans.

6. As Found by the Court of Appeals, the Evidence Fails to Prove That Other Lenders Were Prevented by Any Cost Advantage Enjoyed by Petitioners From Making 100% or Equally Favorable Land Loans.

Fortner's brief (pp. 24-25) broadly claims:

> "We established the Credit Corporation's unique economic ability to provide a 100% land acquisition and development loan at cheap rates as a part of the deliberate scheme of the petitioners. We established the economic barriers due to risk factor as well as legal barriers to many lenders and actually established what amounted to a cost advantage."

As noted in petitioners' principal brief, the Court of Appeals found that "there is no showing in the record that there were lenders in or out of Louisville having higher costs or lower profitability than the Credit Corporation" (A 1382), and after the second trial that court concluded that "the trial court failed to make any findings on this issue and [Fortner] does not contend on appeal that a cost advantage was established." Rather, as the Court of Appeals concluded, the trial judge's findings (A 1601) were merely that "other lending institutions were not making such high percentage loans only because of their unwillingness to take the risk involved." (A 1768)

In a belated effort to avoid the fact that the evidence and its own proposed findings adopted verbatim by the

trial judge wholly fail to show that petitioners had any cost advantage, unique or otherwise, in the credit market, Fortner now argues (pp. 27-28) that the Homes Division guaranty of special land financing, including Fortner's, gave the Credit Corporation "a cost advantage not available to other lenders" at "the given time in question in this litigation." Even its own findings, adopted by the trial court, however, do not purport to equate the Homes Division guaranty with any cost advantage in the credit market. (A 1580, 1590, 1595, 1600) Moreover, the evidence of record and elementary logic would refute any such finding or conclusion.

First, the Homes Division guaranty, when considered against the undisputed fact that the Credit Corporation had lower profitability than many, if not most, other lenders, confirms the Credit Corporation's overall cost disadvantage rather than demonstrating that it had any cost advantage. Thus, even though the Credit Corporation was insulated by its affiliate against loss on the guaranteed special land loans, its rate of profit, as the Court of Appeals noted, was (1) shown to be substantially lower than that of many lenders and (2) not shown to be as high as that of any other lender.[20] (A 1501-12) Indeed, both the Court of Appeals (A 1381) and Justice Fortas of this Court (394 U.S. at 525) stated that the record justified the conclusion that the Credit Corporation, while not operating at a loss, had comparatively low profits. At the same time, there is no evidence that the special land loans were or

20. Fortner's expert, Professor Masten, testified that the Credit Corporation "was only about half as profitable as the average commercial bank" and that it was "not a particularly profitable operation" —it was "relatively unprofitable." (A 1644, 1647, 1696)

would have been unprofitable without the Homes Division guaranty. Instead, after Fortner's financing traditional lending sources in Louisville promptly began and continued to make 100% loans.

Second, even apart from the fact that the record shows that notwithstanding the guaranty the Credit Corporation had a lower rate of profit than traditional lenders, if losses had in fact been incurred on any financing underwritten by the Homes Division, then those losses would be borne by the Homes Division and charged against its operations in the housing market, the tied product market. The Homes Division's willingness to bear any losses on special land financing in order to promote the sale of its houses, therefore, in no way represented any economies of scale, lower costs or higher rate of profit enjoyed by the Credit Corporation in the tying credit market, as this Court held would be necessary to prove economic power over credit. (394 U.S. at 505-506, 509) Significantly, although apprised of the Homes Division guaranty, Justice Black and the majority of this Court in no way indicated that it evidenced or even suggested the possibility of economic power over credit.

While Fortner concedes (p. 28) that the Homes Division guaranty "was not a cost advantage in the traditional sense," it urges (pp. 22-23, 27) an even more fanciful theory of cost advantage which the Credit Corporation allegedly might have had but concededly did not. Adverting to the fact that the bulk of the funds loaned by the Credit Corporation were first borrowed from commercial

banks at the prime rate (a potent cost disadvantage), Fortner states:

> "[The trial court] found that United States Steel Corporation *could* have used its own funds which were readily available to finance the Credit Corporation directly, which funds would have cost the Credit Corporation nothing. Credit Corporation quite clearly *would* have been at a distinct cost advantage if United States Steel Corporation had funded Credit Corporation entirely at a no interest basis which could easily have been done. • • • [The Credit Corporation] *could* have been financed entirely by cash from United States Steel Corporation's vast wealth, and it clearly *would have had a cost advantage.*"

Fortner's argument and its proposed findings adopted by the trial judge embodying that argument are an admission that U.S. Steel did not endow the Credit Corporation with any cost advantage by pouring interest-free equity capital into the finance subsidiary, even if such theoretical sleight-of-hand based upon the assumption of "free money" had any economic validity in the real world.[21] Instead, as the evidence shows, the Credit Corporation's prime rate cost of obtaining the funds it then loaned was substantially higher than that of the traditional lending institutions, such as commercial banks, from which it had to borrow and which obtain their funds at far less than the prime rate.

Moreover, the contention that the Credit Corporation theoretically could have been given a cost advantage by

21. As even Professor Masten testified, "Certainly a corporation like U.S. Steel could have used the funds in some other area more profitably." (A 1696) U.S. Steel obviously is accountable to its stockholders and owes them a return on investment inconsistent with making free money available even to its own subsidiaries when a higher return is available elsewhere.

substituting U.S. Steel's equity capital is not only contrary to what in fact was done but also betrays a basic misconception as to why a successful manufacturing company undertaking a finance business does so through a credit subsidiary—the same purpose which the undisputed evidence shows prompted U.S. Steel's *modus operandi* with the Credit Corporation. (A 957, 962, 982) The salient consideration is that U.S. Steel chose the cheapest, lowest cost means available to obtain the funds which the Credit Corporation loaned, and even then it operated at a cost disadvantage. Thus, borrowing through a finance subsidiary, a manufacturing parent can obtain from commercial banks and other primary financing sources larger sums in relation to its committed equity than it could by itself, because those prime lending sources accept a higher debt-to-equity ratio for finance company borrowers. This allows the generation of more money for loans at lower net cost to the overall enterprise (parent and credit subsidiary), because the parent need not divert capital it can devote to its own more profitable uses.[22]

In conclusion, the record is devoid of testimony (even by Professor Masten) or other evidence that conventional lenders in Louisville were *unable* profitably to offer 100% or comparable land loans in 1960 and 1961, however Fortner now characterizes the trial testimony (but without record citations). Taking the testimony in its broadest possible ambit, the several witnesses stated only that they knew of no traditional lending sources that were making 100% loans

22. See Note, "Credit as a Tying Product," 69 Col. L. Rev. 1434, 1449-1450 (1969); *cf.*, General Motors Acceptance Corp., Quarterly Report (June 30, 1969).

at that particular time, *i.e.*, such loans were then *unavailable.* As the Court of Appeals observed, even Fortner's findings adopted by the trial judge do not conclude that any other lender was precluded by any cost disadvantage or otherwise from profitably matching the Credit Corporation's alleged 100% financing of Fortner. To the contrary, those findings simply conclude:

> "[The Credit Corporation] was willing to take higher risks because it had a purpose or motive which other conventional lenders did not have, namely: to enable its parent, United States Steel Corporation, to sell prefabricated house packages. While some conventional lenders might be willing to take higher risks than others, the evidence is that during the period of time in question in this lawsuit no conventional lenders were *willing* to take the degree of risk which Credit Corporation was voluntarily and deliberately willing to take for its purposes." (A 1601)

On such a record, petitioners submit that this Court's mandate was disregarded by both the trial judge and by the Court of Appeals, which erroneously held that Fortner could "prevail even if it failed to show that other lending institutions were prevented from offering a loan on equally favorable terms * * *." (A 1767)

7. In Erroneously Ignoring the Undisputed Fact That Conventional Louisville Lenders, Earlier Unwilling to Risk Lower Profits, Were Stimulated to Engage in 100% Financing, the Courts Below Disregarded This Court's Mandate.

In their principal brief, petitioners have urged that the failure to offer any evidence that other lenders were unable profitably to make 100% or comparable land loans fatally undermines Fortner's contentions as to economic power over credit. Petitioners have also noted (pp. 40-43) that this failure of proof is emphasized by the uncontradicted evidence that, as the Court of Appeals stated, "soon after [Fortner] negotiated its financing terms with the defendants for 100% financing, traditional lending agencies in Louisville indeed began offering loans upon the same basis." (A 1380)

Fortner attempts to minimize the fact that traditional lending sources in Louisville promptly responded with 100% loans by urging (p. 38) that there was only "some limited evidence" of that fact. Significantly, however, such testimony was not only undisputed but it came primarily from Fortner's own witnesses, and it was unlimited in breadth and scope—not confined to just a few specifically identified instances or points in time.[23] More importantly, the fact that conventional lending sources began offering 100% loans soon after Fortner's financing was never in issue. The only dispute was with respect to whether 100% loans were available from other lenders even at the time of the financing of Fortner. From essentially the beginning of the litigation, Fortner's own witnesses conceded that within less than a year conventional sources were making such loans.

23. *E.g.*, A 421-22, 429-30, 821-23, 839-44, 847, 868-69, 1661-62; 1970 Transcript, Vol. XVI, pp. 19-20.

Thus, at least as early as the summary judgment motion in 1966, it was clear that Fortner was claiming merely that 100% land loans were not elsewhere available only at the time of its financing in 1960 and 1961. For example, as Fortner's brief concedes (p. 39), its witness, Edwin D. Horn, whose affidavit was before this Court,[24] claimed only that "during the period 1959 through 1962" such financing was "not available." He conceded that thereafter his company, the largest mortgage concern in Louisville, and other lenders there were "forced to offer to their customers similar 100% financing" because of the Fortner loans and others like them, including those by prefabricated house manufacturers other than the Homes Division.

As Fortner concedes in its brief here (p. 39), in adopting its proposed findings the trial judge "chose to ignore" this crucial fact. On the second appeal, the Court of Appeals gave it no weight. Petitioners submit that no single fact could be more significant in determining whether competing lenders had the *ability* to offer the Credit Corporation's alleged 100% terms than showing that they simply *chose* not to incur the risk of lower profit on such loans until stimulated by competition to do so. That conclusion and the fact that this Court's mandate has been misunderstood or ignored below are buttressed by the trial court's finding (A 1601), adopted by the Court of Appeals (A 1768), that "other lending institutions were not making

24. See Vol. I, Joint Appendix, at pp. 294a-295a, in No. 306, October Term, 1968.

such high percentage loans only because of their unwillingness to take the risk involved'' inasmuch as they would not, as Fortner admitted in its brief before the Court of Appeals (p. 39), take the ''chance of the loans not being profitable.''

Conclusion

For all of the reasons set forth here and in their principal brief, petitioners urge that the record, taken in its entirety and drawing every reasonable inference in favor of respondent, demonstrates that respondent has failed to make out a *prima facie* case of the economic power over credit necessary to establish a *per se* tying violation or any other violation of either Sections 1 or 2 of the Sherman Act and, therefore, that the judgment below should be reversed and the entry of a judgment dismissing the complaint should be ordered by this Court.

Respectfully submitted,

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Appendix

Throughout this litigation and again in its brief here (pp. 7-8), Fortner has urged and the trial court found in adopting Fortner's proposed findings that ''millions of dollars of sales'' resulted from ''the tie-in * * * agreement complained of * * *'' in this suit. (A 1578) In claiming that the Credit Corporation's loans to others than Fortner contained the tie-in provision *which is the subject matter of this suit* * * *'' and induced the purchase of Homes Division houses, these and similar contentions by Fortner and related findings by the trial court (A 1589-90, 1601) are wholly without support in the record. The disposition of this case on the points of law covered in their briefs would be the same even if the record supported Fortner on these and similar factual contentions. Petitioners nonetheless address themselves to these contentions in this appendix, because Fortner's efforts to magnify and dramatize the allegedly pervasive nature of its claims and proof might otherwise unduly color what in fact is involved here.

Concededly as much as 70% of the Homes Division's sales were accompanied by Credit Corporation financing of some kind. Substantially all of that financing was conditioned upon use of the funds to buy or construct Homes Division houses or, in some instances, to acquire or develop land on which such houses would be placed.[1] There is no

1. The Credit Corporation's loan *commitments* (not the lesser amount actually borrowed against those commitments) for all types of financing, including the purchase and erection of Homes Division houses as well as for land acquisition or development, were at least $19 million in each of the years 1960 through 1962, as stated by Fortner (p. 7) and found below. (A 1590) As the facts of the loan transactions with Fortner demonstrate, however, the commitment

(footnote continued on next page)

evidence, however, as to what proportion of sales financed by the Credit Corporation involved *land* financing (whether regular, special, or both), as opposed to financing for the purchase and erection of houses, which is unchallenged in this action.

Consequently, there is absolutely no factual basis for Fortner's claim (p. 7) that essentially "all of [the Credit Corporation's] loans were conditioned upon the tie-in provisions complained of by Fortner'"[2] and that "68% to 70% of all sales were accounted for by loans involving the tie-in," because Fortner complains only of 100% land financing or of land loans shown to be on uniquely favorable terms not available elsewhere. In other words, not even *all land* financing is challenged, but only those land loans which were assertedly on uniquely favorable terms, thus allegedly justifying application of the *per se* tying rule. Fortner offered evidence only that 100% land financing was unavailable in Louisville until 1962. There is no proof of the terms extended to any builder other than Fortner or that such terms were in any way "unique" in comparison with the land financing available in the other areas where, and at the times when, such financing was granted.

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represented by loan agreements at any point in time would substantially exceed the volume of loans outstanding, because the Credit Corporation was obligated to advance funds only on prescribed progress schedules and amounts advanced similarly were to be repaid on a progress basis before the terminal date of the commitment, even if the borrower ultimately took down the full amount of the commitment promised him. (A44-74)

2. This Court made it clear that the only relevant financing and house sales are those "tied by the sales policy under challenge * * *." (394 U.S. at 502)

Similarly, the record does not support the finding below that the tie-in agreements "complained of" restrained commerce by "resulting in millions of dollars of sales" by the Homes Division. With the sole exception of the claim that but for the financing Fortner would not have bought petitioners' houses, there is not a scintilla of evidence as to why any other Homes Division customers bought its houses or that it was for any reason other than that they affirmatively found the houses attractive and purchased them on their own merits. There is no basis for finding that other customers were induced by uniquely favorable financing terms to buy the houses (even if that were proof of power over credit) or that any competitors of the Homes Division were foreclosed because of such financing.

Fortner correctly cites the record in stating (p. 7), "Land financing loans outstanding alone amounted to $5,372,000 at the end of 1960 (A 1353), while house package sales amounted to $6,747,353 (A 1199)." The implication that petitioners were making land loans of such favorable terms as to be unavailable elsewhere in amounts roughly equivalent to their house sales, however, is not supported by the evidence. The land loans outstanding at the end of 1960 included loans made in earlier years as well and, therefore, were not properly to be compared solely against house sales in that year. More importantly, however, the land loan figure cited included all types of land loans, including the "regular" category as to which there is no challenge. There is no showing that "special" land loans, let alone 100% or otherwise allegedly uniquely favorable loans, even

constituted a significant proportion of the total loan figure cited.

In similar vein, Fortner implies (p. 8) that petitioners' allegedly uniquely favorable land loans annually exceeded the volume of house sales in the same year:

> "A more significant fact is that the original amounts of the loans dated prior to the end of 1961 [guaranteed by the Homes Division and therefore in the special land loan category] total $7,738,000 (A 1273-1274), well in excess of the total land financing loans outstanding at the end of 1961 of $5,918,000 [and of house sales of $5,051,992 (A 1199) in that year]."

The purported comparison, however, is spurious. First, as comparison of the loan figure shown for Fortner in the cited exhibit with the lesser amount actually taken by Fortner demonstrates, the $7,738,000 figure represented commitments by the Credit Corporation, not the amount of special land loans outstanding at any time or even necessarily ever advanced to the borrowers. Second, the cited exhibit and the Fortner loans listed there demonstrate that the special land loan commitments outlined dated back to as early as 1959. They were not, therefore, properly comparable with house sales only in 1961. Finally, while the listed commitments were admittedly in the "special" land loan category, there is no evidence that they were 100% commitments, that they were commitments on terms uniquely favorable by comparison with loans available from other sources in the areas and at the times they were made, or that any other builder was induced by those commitments to build petitioners' houses rather than others.